

Condensed Interim Consolidated Financial Statements of

SOUTHERN ENERGY CORP.

For the three and six months ended June 30, 2024 and 2023

(unaudited)

(U.S. Dollars)

SOUTHERN ENERGY CORP.

Condensed Interim Consolidated Statement of Financial Position (unaudited)



| (in thousands of U.S. Dollars) | June 30, 2024 | December 31, 2023 |
|--|------------------|----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 1,522 | \$ 3,112 |
| Accounts receivable and other | 2,326 | 2,134 |
| Prepaid expenses and deposits | 1,160 | 1,089 |
| Derivative assets (Note 9) | 636 | 1,022 |
| | 5,644 | 7,357 |
| Property, plant and equipment (Note 3) | 53,550 | 59,608 |
| Right-of-use assets | 46 | 105 |
| Derivative assets (Note 9) | 29 | 235 |
| Total assets | \$ 59,269 | \$ 67,305 |
| Liabilities and Equity | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | 2,586 | 5,535 |
| Royalties payable (Note 10) | 6,331 | 6,362 |
| Current portion of lease liabilities | 55 | 121 |
| Current portion of long-term debt (Note 5) | 3,021 | 4,657 |
| Convertible debentures (Note 6) | 3,092 | 3,196 |
| Derivative liabilities (Note 9) | 149 | 10 |
| | 15,234 | 19,881 |
| Long-term liabilities | | |
| Derivative liabilities (Note 9) | 917 | 37 |
| Long-term debt (Note 5) | 14,807 | 12,659 |
| Decommissioning provisions (Note 4) | 8,081 | 8,917 |
| Total liabilities | 39,039 | 41,494 |
| Shareholders' equity (Note 7) | | |
| Share capital | 79,892 | 79,764 |
| Equity component of convertible debenture | 245 | 245 |
| Warrants | 351 | 351 |
| Contributed surplus | 7,704 | 7,569 |
| Deficit | (67,155) | (61,412) |
| Accumulated other comprehensive loss | (807) | (706) |
| | 20,230 | 25,811 |
| Total liabilities and shareholders' equity | \$ 59,269 | \$ 67,305 |

(See accompanying Notes to the Condensed Interim Consolidated Financial Statements)

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Condensed Interim Consolidated Statement of Loss & Comprehensive Loss (unaudited)

| (in thousands of U.S. Dollars, except for per share amounts) | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|-------------------|------------------------------|-------------------|
| | 2024 | 2023 | 2024 | 2023 |
| Revenues | | | | |
| Petroleum and natural gas revenue (Note 11) | \$ 3,889 | \$ 3,741 | \$ 8,683 | \$ 8,930 |
| Royalties | (789) | (649) | (1,733) | (1,709) |
| | <u>3,100</u> | <u>3,092</u> | <u>6,950</u> | <u>7,221</u> |
| Expenses | | | | |
| Production and operating | 1,445 | 1,491 | 3,097 | 2,904 |
| Transportation | 375 | 296 | 769 | 357 |
| Depletion, depreciation and amortization (Note 3) | 1,774 | 2,367 | 3,854 | 4,703 |
| Gain on derivatives (Note 9) | (69) | (112) | (210) | (211) |
| Loss on debt modification (Note 5) | 53 | - | 1,379 | - |
| Loss on sale of assets (Note 3) | 219 | - | 219 | - |
| Financing, net (Note 12) | 760 | 583 | 1,553 | 845 |
| General and administrative | 1,054 | 1,713 | 2,006 | 2,663 |
| Share-based compensation (Note 7) | 168 | 394 | 231 | 534 |
| Transaction costs | - | 1 | - | 199 |
| (Gain) loss on foreign exchange | (57) | 126 | (205) | 114 |
| | <u>5,722</u> | <u>6,859</u> | <u>12,693</u> | <u>12,108</u> |
| Total net loss earnings for the period | (2,622) | (3,767) | (5,743) | (4,887) |
| Currency translation adjustment | (27) | 51 | (101) | 34 |
| Comprehensive loss income for the period | <u>\$ (2,649)</u> | <u>\$ (3,716)</u> | <u>\$ (5,844)</u> | <u>\$ (4,853)</u> |
| Net loss per common share (Note 8) | | | | |
| Basic | \$ (0.02) | \$ (0.03) | \$ (0.03) | \$ (0.04) |
| Diluted | \$ (0.02) | \$ (0.03) | \$ (0.03) | \$ (0.04) |

(See accompanying Notes to the Condensed Interim Consolidated Financial Statements)

SOUTHERN ENERGY CORP.



Condensed Interim Consolidated Statement of Changes in Shareholders' Equity (unaudited)

| (in thousands of U.S. Dollars, except share amounts) | Common Shares | Shareholders' Capital | Equity Component of Convertible Debentures | Warrants | Contributed Surplus | Deficit | Accumulated Other Comprehensive Income (Loss) | Shareholders' Equity |
|---|------------------|--------------------------|--|----------|------------------------|------------|--|-------------------------|
| Balance, December 31, 2022 | 138,056,910 | \$ 75,271 | \$ 245 | \$ 2,154 | \$ 5,117 | \$(14,595) | \$ (790) | \$ 67,402 |
| Shares issued, net (Note 7) | 984,375 | 295 | - | (62) | - | - | - | 233 |
| Share-based compensation | - | - | - | - | 451 | - | - | 451 |
| Net loss | - | - | - | - | - | (4,887) | - | (4,887) |
| Other comprehensive income | - | - | - | - | - | - | 34 | 34 |
| Balance, June 30, 2023 | 139,041,285 | \$ 75,566 | \$ 245 | \$ 2,092 | \$ 5,568 | \$(19,482) | \$ (756) | \$ 63,233 |
| Balance, December 31, 2023 | 165,718,160 | \$ 79,764 | \$ 245 | \$ 351 | \$ 7,569 | \$(61,412) | \$ (706) | \$ 25,811 |
| Shares issued, net (Note 7) | 779,273 | 128 | - | - | - | - | - | 128 |
| Share-based compensation | - | - | - | - | 135 | - | - | 135 |
| Net loss | - | - | - | - | - | (5,743) | - | (5,743) |
| Other comprehensive income | - | - | - | - | - | - | (101) | (101) |
| Balance, June 30, 2024 | 166,497,433 | \$ 79,892 | \$ 245 | \$ 351 | \$ 7,704 | \$(67,155) | \$ (807) | \$ 20,230 |

(See accompanying Notes to the Condensed Interim Consolidated Financial Statements)

SOUTHERN ENERGY CORP.

Condensed Interim Consolidated Statement of Cash Flows (unaudited)



| (in thousands of U.S. Dollars) | Three months ended | | Six months ended | |
|---|--------------------|------------|------------------|------------|
| | June 30, | | June 30, | |
| | 2024 | 2023 | 2024 | 2023 |
| Operating activities | | | | |
| Total net loss for the period | \$ (2,622) | \$ (3,767) | \$ (5,743) | \$ (4,887) |
| Changes in non-cash items: | | | | |
| Depletion, depreciation and amortization (Note 3) | 1,774 | 2,367 | 3,857 | 4,685 |
| Financing expense | 770 | 605 | 1,572 | 1,019 |
| Unrealized loss (gain) on derivatives (Note 9) | 464 | (89) | 1,611 | (101) |
| Unrealized (gain) loss on foreign exchange | (56) | 124 | (194) | 129 |
| Loss on debt modification | 53 | - | 1,379 | - |
| Loss on disposition | 219 | - | 219 | - |
| Share-based compensation (Note 7) | 168 | 394 | 231 | 534 |
| Decommissioning provisions liabilities settled (Note 4) | (6) | (8) | (6) | (8) |
| Changes in non-cash working capital | (913) | 200 | (544) | 1,919 |
| Net cash (used) provided by operating activities | (149) | (174) | 2,382 | 3,290 |
| Investing activities | | | | |
| Capital expenditures | (60) | (2,005) | (329) | (36,897) |
| Acquisitions | - | (3,287) | - | (3,287) |
| Proceeds from dispositions | 1,360 | - | 1,360 | - |
| Changes in non-cash working capital | (451) | (13,273) | (2,830) | 22 |
| Net cash provided (used) by investing activities | 849 | (18,565) | (1,799) | (40,162) |
| Financing activities | | | | |
| Proceeds from share issuances, net | - | 7 | - | 233 |
| Paydown of long-term debt (Note 5) | (330) | (1,000) | (745) | (1,334) |
| Draw on credit facility (Note 5) | - | 11,500 | - | 13,500 |
| Payment of interest | (671) | (886) | (1,268) | (1,157) |
| Finance lease payments | (35) | (30) | (72) | (65) |
| Transaction costs on debt refinance | (45) | (11) | (52) | (11) |
| Changes in non-cash working capital | 62 | (407) | (5) | (405) |
| Net cash (used) provided by financing activities | (1,019) | 9,173 | (2,142) | 10,761 |
| Net decrease in cash and cash equivalents | (319) | (9,566) | (1,559) | (26,111) |
| Effect of foreign exchange rate changes | (3) | 4 | (31) | 10 |
| Cash and cash equivalents, beginning of period | 1,844 | 11,811 | 3,112 | 28,350 |
| Cash and cash equivalents, end of period | \$ 1,522 | \$ 2,249 | \$ 1,522 | \$ 2,249 |

(See accompanying Notes to the Condensed Interim Consolidated Financial Statements)

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Notes to the Condensed Interim Consolidated Financial Statements (unaudited)
Amounts in thousands of U.S. Dollars, except for per share amounts

1. Reporting Entity and Nature of Operations

Southern Energy Corp. (“Southern” or the “Company”) is a petroleum and natural gas exploration and production company. Southern has a primary focus on acquiring and developing conventional natural gas and light oil resources in the Southeast Gulf States of Mississippi, Louisiana, and East Texas.

Southern’s head office is located in Calgary, Alberta, Canada. Southern trades on the TSX Venture Exchange (“TSXV”) under the trading symbol “SOU” and on the AIM market of the London Stock Exchange (“AIM”) under the trading symbol “SOUC”. The condensed interim consolidated financial statements were authorized for issue by the Board of Directors on August 20, 2024.

2. Basis of Presentation

a) Principles of Reporting and Consolidation

The condensed interim consolidated financial statements of Southern include the accounts of all domestic and foreign subsidiaries. Wholly-owned subsidiaries included in the Company’s accounts include Southern Energy Corp., Southern Energy Corp (Delaware), Southern Energy Operating, LLC, Southern Energy CMS, LLC, Southern Energy LA, LLC and Southern Energy BWB, LLC. Southern accounts for joint operations by recognizing the Company’s share of assets, liabilities, income and expenses. All intercompany balances and transactions have been eliminated.

These condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting of the International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”). The condensed interim consolidated financial statements use the accounting policies which the Company applied in its annual consolidated financial statements for the year ended December 31, 2023. These condensed interim consolidated financial statements should be read in conjunction with Southern’s consolidated financial statements for the year ended December 31, 2023, which are available on SEDAR+ at www.sedarplus.ca or on Southern’s website at www.southernenergycorp.com. These condensed interim consolidated financial statements are presented in United States dollars (“U.S. dollars”). All financial information presented has been rounded to the nearest thousand unless otherwise indicated.

b) Adopted Accounting Changes

Amendments to IAS 1, Presentation of Financial Statements

Southern adopted the amendments to IAS 1 Presentation of Financial Statements effective January 1, 2024. The amendments are related to the classification of liabilities as current and non-current. Southern does not believe these amendments have any impact on the Company’s financial statements or disclosures.

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3. Property, Plant and Equipment

The following table presents the reconciliation of the beginning and ending amounts of our PP&E balances including accumulated depletion, depreciation and amortization:

| | Petroleum and Natural | | Total |
|---|--------------------------|---------------|------------------|
| | Gas Assets | Other | |
| Net book value as at December 31, 2023 | \$ 59,423 | \$ 185 | \$ 59,608 |
| Additions | 323 | 6 | 329 |
| Acquisitions, including decommissioning costs | 32 | - | 32 |
| Dispositions | (1,579) | - | (1,579) |
| Change in decommissioning provision (Note 4) | (1,036) | - | (1,036) |
| Depletion, depreciation and amortization | (3,774) | (27) | (3,801) |
| Foreign exchange | 1 | (4) | (3) |
| Net book value as at June 30, 2024 | \$ 53,390 | \$ 160 | \$ 53,550 |

Additions

For the six months ended June 30, 2024, Southern incurred \$0.3 million of capital additions related to the development of the Central Mississippi Cash Generating Unit ("CMS CGU").

Dispositions

In Q2 2024, Southern sold excess equipment for net proceeds of \$1.4 million, resulting in a loss on disposition of \$0.2 million in the Condensed Interim Consolidated Statement of Loss and Comprehensive Loss.

Depletion and depreciation

For the three and six months ended June 30, 2024, the Company recorded depletion expense of \$1.7 million and \$3.8 million, respectively. In the calculation of depletion expense, an estimated \$161.8 million of future development costs associated with the proven plus probable reserves were included.

Impairment and impairment recovery

At the end of each reporting period, the Company performs an assessment to determine whether there are any indications of impairment for the CGUs that comprise petroleum and natural gas properties. As at June 30, 2024, Southern did not identify any indicators of impairment or impairment recovery for any of its CGUs.

4. Decommissioning Provisions

The Company's decommissioning provisions result from its ownership interest in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The total decommissioning

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provision is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The total estimated, inflated undiscounted risked cash flows required to settle the provision, is approximately \$19.7 million at June 30, 2024 (December 31, 2023 – \$20.3 million). The decommissioning provision was inflated using a rate of 2.3% (December 31, 2023 – 2.4%) and discounted using a risk-free interest rate of 4.36% at June 30, 2024 (December 31, 2023 – 3.9%). These obligations are to be settled based on the economic lives of the underlying assets, which currently extend up to 50 years into the future and will be funded from general corporate resources at the time of abandonment. The following table presents the reconciliation of the beginning and ending aggregate carrying amounts of legal obligations associated with the retirement of property, plant and equipment:

| | 2024 |
|---|-----------------|
| Balance, beginning of year | \$ 8,917 |
| Liabilities acquired | 32 |
| Changes in estimates | (1,036) |
| Liabilities settled | (6) |
| Accretion expense | 175 |
| Effect of foreign exchange rate changes | (1) |
| Balance, end of period | \$ 8,081 |
| Long term liability | \$ 8,081 |

5. Long-term Debt

Southern had the following long-term debt obligations outstanding as at the dates indicated:

| | As at Jun 30, 2024 | As at Dec 31, 2023 |
|---|---------------------------|---------------------------|
| Current portion of senior secured term loan | \$ 3,021 | \$ 4,985 |
| Long-term portion of senior secured term loan | 15,263 | 12,879 |
| Unamortized transaction costs | (456) | (548) |
| Total Long-Term Debt | \$ 17,828 | \$ 17,316 |

Southern Energy Corporation (Delaware), one of the wholly-owned subsidiaries of Southern, held the existing senior secured term loan ("Credit Facility") at June 30, 2024. The Credit Facility is comprised of Tranche A of \$5.5 million that was advanced at closing on April 30, 2021 and Tranche B of \$31.5 million with an availability until December 31, 2026. Effective February 28, 2024, interest on the Credit Facility is 15% per annum (previously 12% per annum) on amounts outstanding and includes a 1% per annum standby fee on the unused portion of Tranche B, both paid monthly in arrears on the last day of the month. The Credit Facility is secured against the oil and gas properties of Southern and matures on December 31, 2026. As at June 30, 2024, Southern had \$17.1 million drawn on the Credit Facility and \$10.0 million available from Tranche B.

Effective February 28, 2024, Southern entered into the sixth amendment to the Credit Facility (the "Sixth Amendment"). The Sixth Amendment included an extension of the maturity of the Credit Facility to December 31, 2026, reset the debt service coverage ratio ("DSCR") (as defined below) covenant calculation to an annualized basis beginning in Q1 2024, reduced the repayments based on a free cash flow ("FCF") grid (as described below) and increased the fixed per annum coupon from 12% to 15% per

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annum. The amendment also paused the monthly repayment of the principal amount outstanding (as described below) for the period from February 1, 2024 to September 30, 2024. The Sixth Amendment was accounted for in Q1 2024 as a debt modification under IFRS 9, resulting in a non-cash loss of \$1.3 million in the Condensed Interim Consolidated Statement of Loss and Comprehensive Loss.

Quarterly positive FCF (as described below) repayments are based on a FCF grid whereby quarterly repayments are X% of the preceding quarter where X is equal to 30% if the ACR (as defined below) is < 3.0x or DSCR (as defined below) is < 1.4x; or X is equal to 0% if the ACR is > 5.0x and DSCR > 1.7x; otherwise is 15%.

The Credit Facility includes a monthly repayment of the principal amount outstanding computed as the sum of: (a) outstanding amount multiplied by 1/A, where A equals the number of whole or part months remaining to the maturity date plus 24 months; and (b) on the last day of the second month following each fiscal quarter, the amount determined by the FCF grid (as described above). FCF is calculated as Earnings Before Interest, Taxes, Depreciation, Amortization, and Impairment (“EBITDAX”), less the aggregate of the Credit Facility principal and interest payments.

Below are the financial covenant calculations for the Credit Facility for June 30, 2024 and December 31, 2023:

| Financial covenant | Limit | As at Jun 30, 2024 | As at Dec 31, 2023 |
|-----------------------------|--------------|-------------------------------|-------------------------------|
| Asset Coverage ratio | Minimum 2.00 | 2.12 | 2.48 |
| Debt Service Coverage ratio | Minimum 1.25 | 1.42 | 0.43 |

The asset coverage ratio (“ACR”) of at least 2:1 is calculated as the ratio of the net present value of proved developed producing oil and gas properties as determined by an independent qualified engineer, using a price deck based on the forward commodity prices, discounted at 12% to the principle amount outstanding under the Credit Facility.

The DSCR of greater than 1.25:1 is the ratio of EBITDAX to scheduled principal payments and interest expense.

On December 19, 2023, Southern obtained a waiver for the DSCR for the fiscal quarter ending December 31, 2023.

As at June 30, 2024, Southern was in compliance with the above covenants.

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6. Convertible Debentures

| | Number of Convertible Debentures | Liability Component (\$000s) | Equity Component (\$000s) |
|---|--|------------------------------------|---------------------------------|
| Balance at December 31, 2023 | 4,286 | \$ 3,196 | \$ 245 |
| Accretion of discount | - | 43 | - |
| Net impact of debt modification | - | (40) | - |
| Effect of foreign exchange rate changes | - | (107) | - |
| Balance at June 30, 2024 | 4,286 | \$ 3,092 | \$ 245 |

On June 26, 2024, Southern amended its outstanding convertible unsecured subordinated debentures ("Debentures") to extend the maturity date of the 4,286 outstanding Debentures by one year to June 30, 2025, and increase the interest on the Debentures from 8.00% to 10.00% per annum commencing on June 30, 2024 pursuant to a second supplemental debenture indenture.

In connection with the second supplemental debenture indenture the Company issued a total of 1,863,478 Common Share purchase warrants ("Warrants") to the holders of the Debentures ("Debentureholders") for no additional consideration, with each Warrant entitling the Debentureholder to purchase one Common Share of the Company at a price of CAD\$0.25 for a period of 12 months from the date of issuance. The Warrants, and any Common Shares issued upon the exercise of the Warrants, are subject to a statutory four month and one day hold period from the date of issuance.

At June 30, 2024, the convertible debentures were classified as a current liability as they have a maturity date of June 30, 2025.

On July 2, 2024, the June 30, 2024 accrued interest payment was settled in-kind through the issuance of 745,391 new Common Shares. The number of Common Shares issued was equal to the amount of interest, divided by the volume weighted average trading price per Common Share for the 20 consecutive trading days ending on the fifth trading day preceding June 30, 2024.

7. Shareholders' Equity

Share Capital

The authorized share capital of the Company consists of an unlimited number of Common Shares and an unlimited number of preferred shares.

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The following table reflects the Company's outstanding Common Shares at June 30, 2024 and December 2023:

| | Number of Shares | Share Capital (\$000s) |
|---|-----------------------------|---------------------------------------|
| Balance as at December 31, 2023 | 165,718,160 | \$ 79,764 |
| Issuance of Common Shares to settle convertible debenture interest (Note 6) | 779,273 | 128 |
| Balance as at June 30, 2024 | 166,497,433 | \$ 79,892 |

On January 2, 2024, the December 31, 2023 accrued interest payment was settled in-kind through the issuance of 779,273 new Common Shares. The number of Common Shares issued was equal to the amount of interest, divided by the volume weighted average trading price per Common Share for the 20 consecutive trading days ending on the fifth trading day preceding December 31, 2023.

Warrants

In connection with the fifth amendment to the Credit Facility, the Company has agreed to extend the term of the outstanding Common Share purchase warrants ("Bonus Warrants") previously issued to the lender from April 30, 2024 until August 31, 2025. There are 3,906,250 remaining Bonus Warrants with an exercise price of CAD\$0.40.

Stock Option Plan

Under the Company's security based compensation arrangement, which includes the stock option plan and share award incentive plan, the Company may grant options or share awards to its directors, officers, employees and consultants up to a maximum of 10% of the issued and outstanding Common Shares at the time of the grant, with a maximum of 5% of the Company's issued and outstanding shares reserved for any one person on a yearly basis. The maximum stock option term is 10 years from the grant date with vesting terms set at the discretion of the board of directors.

The following table reflects the Company's outstanding common stock options at June 30, 2024 and December 31, 2023:

| | Number of stock options | Weighted average exercise price (CAD) |
|---------------------------------|------------------------------------|--|
| Balance at December 31, 2023 | 7,114,375 | \$ 0.86 |
| Expired | (2,200,000) | 0.80 |
| Balance at June 30, 2024 | 4,914,375 | \$ 0.89 |

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The following table summarizes information regarding stock options outstanding as at June 30, 2024:

| Exercise Price (CAD\$/share) | Number of options outstanding (000s) | Weighted average remaining terms (years) | Weighted average exercise price for options outstanding (CAD\$/share) | Number of options exercisable (000s) | Weighted average exercise price for options exercisable (CAD\$/share) |
|---------------------------------|---|---|--|---|--|
| \$0.39 - \$1.01 | 4,914 | 3.0 | \$0.89 | 3,816 | \$0.85 |

Southern recognized \$0.1 million of share-based compensation expense relating to stock options during the three and six months ended June 30, 2024, respectively, compared to \$0.2 million and \$0.5 million for the same periods in 2023.

Subsequent to June 30, 2024, Southern issued 3,102,500 stock options as part of the overall compensation and employee retention program.

Share Award Incentive Plan

The following table reflects the Company's outstanding restricted share awards ("RSAs") at June 30, 2024 and December 31, 2023:

| | Number of RSAs |
|---------------------------------|-----------------------|
| Balance at December 31, 2023 | 2,949,657 |
| Released upon cash settlement | (448,597) |
| Balance at June 30, 2024 | 2,501,060 |

Southern recognized \$0.1 million of share-based compensation expense relating to the RSAs during the three and six months ended June 30, 2024, respectively, compared to \$0.2 million and \$0.1 million for the same periods in 2023.

8. Loss Per Share

The following table presents the Company's net loss per share:

| | Three months ended | | Six months ended | |
|--|--------------------|-------------|------------------|-------------|
| | June 30, | | June 30, | |
| | 2024 | 2023 | 2024 | 2023 |
| Net loss | \$ (2,622) | \$ (3,767) | \$ (5,743) | \$ (4,887) |
| Basic and diluted - weighted average Common Shares outstanding | 166,497,433 | 139,039,225 | 166,488,870 | 138,816,406 |
| Net loss per share, basic and diluted | \$ (0.02) | \$ (0.03) | \$ (0.03) | \$ (0.04) |

The calculation of diluted loss per share for the three and six months ended June 30, 2024 excludes the effect of all outstanding share options, Bonus Warrants, convertible debentures and Debenture warrants as they are anti-dilutive.

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9. Financial Instruments and Financial Risk Management

Financial Derivative Contracts

Southern utilizes crude oil and natural gas derivative contracts to mitigate its exposure to commodity price risk associated with future crude oil and natural gas production. Typical derivative contracts could consist of options, in the form of price floors, collars or three-way collars and fixed-price swaps. The derivative financial instruments are recorded on the consolidated statement of financial position as either an asset or a liability measured at fair value. Southern does not apply hedge accounting to its commodity derivative contracts; accordingly, changes in the fair value of these instruments are recognized in the consolidated statement of loss and comprehensive loss in the period of change.

Southern had the following commodity derivative contracts in place as at June 30, 2024:

| Natural Gas | Volume | Pricing |
|-----------------------------------|---------------|----------------------------------|
| <i>Costless Collar</i> | | |
| November 1, 2024 – March 31, 2025 | 1,000 MMBtu/d | NYMEX – HH \$3.50 - \$5.20/MMBtu |
| <i>Fixed Price Swap</i> | | |
| July 1, 2024 – December 31, 2026 | 5,000 MMBtu/d | NYMEX – HH \$3.400/MMBtu |

In Q1 2024, Southern monetized the fixed price swap derivative contracts to take advantage of the positive unrealized gain position, realizing net proceeds of \$1.1 million.

Financial Derivative Contracts Financial Statement Recognition

The Company's financial instruments that were accounted for at fair value as of June 30, 2024 and December 31, 2023 are presented below:

| Comprised of: | As at Jun 30, 2024 | As at Dec 31, 2023 |
|---|---------------------------|---------------------------|
| Current derivative asset | \$ 636 | \$ 1,022 |
| Current derivative liability | (149) | (10) |
| Non-current derivative asset | 29 | 235 |
| Non-current derivative liability | (917) | (37) |
| Net fair value of contracts, end of period | \$ (401) | \$ 1,210 |

Below is a reconciliation of the gain on derivatives from the condensed interim consolidated statement of loss and comprehensive loss:

| | Three months ended June 30, | | Six months ended June 30, | |
|---------------------------------------|--------------------------------|-----------------|------------------------------|-----------------|
| | 2024 | 2023 | 2024 | 2023 |
| Realized gain on derivatives | \$ (533) | \$ (23) | \$ (1,821) | \$ (110) |
| Unrealized loss (gain) on derivatives | 464 | (89) | 1,611 | (101) |
| Gain on derivative instruments | \$ (69) | \$ (112) | \$ (210) | \$ (211) |

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Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

The carrying amount of the Company's cash and cash equivalents and accounts receivable and the positive fair value of any financial derivatives represent the maximum credit exposure.

Cash and cash equivalents

The Company manages the credit exposure related to cash and cash equivalents by selecting financial institutions with high credit ratings and monitors all short-term deposits to ensure an adequate rate of return. Given these credit ratings, management does not expect any counterparty to fail to meet its obligations.

Accounts receivable and other

Substantially all of the Company's accounts receivable are due from purchasers of the Company's petroleum and natural gas production, joint interest partners and government agencies, and are subject to normal industry credit risk.

Significant changes in industry conditions and risks that negatively impact partners' ability to generate cash flow will increase the risk of not collecting receivables. Management of the Company believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

Southern had no provision for doubtful accounts as at June 30, 2024 or December 31, 2023.

Liquidity Risk

Liquidity risk arises through excess financial obligations due over available financial assets at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient capital in order to meet its current and future liquidity requirements. The financial liabilities in the statement of financial position consist of accounts payable, royalties payable, lease liabilities, financial derivative liabilities, convertible debentures and the senior secured credit facility. If financial covenants are not met and the Company is unable to obtain waivers, the debt may become due on demand. This uncertainty may cast doubt with respect to the ability of Southern to continue as a going concern.

Strategies to manage liquidity include, having adequate sources of financing available through its Credit Facilities, estimating future cash flows generated from operations based on reasonable production and pricing assumptions, adding additional commodity derivative contracts, reducing capital spending and utilizing equity to settle interest payments on Convertible Debentures. Southern may also consider sale of non-core petroleum and natural gas assets and excess equipment inventory along with alternative sources of financing. After examining the economic factors that could cause liquidity risk, the Company believes it will have sufficient liquidity to support its operations and meet its financial obligations for at least twelve months. The condensed interim consolidated financial statements have been prepared on a

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going concern basis, which presumes that Southern will continue its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The condensed interim consolidated financial statements do not reflect adjustments and classification of assets, liabilities, revenues and expenses which would be necessary if the Company were unable to continue as a going concern.

Market Risk

Market risk is the risk that changes in market prices relating to currency, commodity prices and interest rates will affect the Company's net earnings, future cash flows, the value of financial instruments, or the fair value of its assets and liabilities. The object of market risk management is to manage and control market risk exposure within acceptable parameters.

To partially mitigate exposure to commodity price risk, Southern entered into various financial derivative instruments. The instruments currently outstanding are described above. As at June 30, 2024, a 10% change in future commodity prices applied against these contracts would have a \$1.6 million impact on net income.

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in interest rates. This risk is mitigated as the Credit Facility has a fixed interest rate.

10. Royalties Payable

As at June 30, 2024, Southern had \$6.3 million (\$6.4 million at December 31, 2023) of non-interest bearing royalty payables related to unresolved title or ownership issues. The royalty payable account is made up of balances due to approximately 6,700 royalty holders with over 95% of the balances outstanding for greater than 120 days. The royalty holders have deficiencies with their accounts that precludes Southern from making payments.

11. Petroleum and Natural Gas Sales

Southern sells its production pursuant to variable price contracts. The transaction price for variable priced contracts is based on the commodity price, adjusted for the quality, location and other factors, whereby each component of the pricing formula can be either fixed or variable, depending on the contract terms. Under the contract, Southern is required to deliver a fixed or variable volume of crude oil, natural gas liquids or natural gas to the contract counterparty. Revenue is recognized when a unit of production is delivered to the contract counterparty. The amount of revenue recognized is based on the agreed transaction price. Revenues are typically collected in the month following production.

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The following table presents Southern’s petroleum and natural gas sales disaggregated by revenue source:

| | Three months ended | | Six months ended | |
|--|--------------------|-----------------|------------------|-----------------|
| | June 30, | | June 30, | |
| | 2024 | 2023 | 2024 | 2023 |
| Commodity sales from production, by product | | | | |
| Crude oil | \$ 816 | \$ 676 | \$ 1,579 | \$ 1,453 |
| Natural gas liquids | 37 | 48 | 75 | 103 |
| Natural gas | 3,036 | 3,017 | 7,029 | 7,374 |
| Total Petroleum and Natural Gas Sales | \$ 3,889 | \$ 3,741 | \$ 8,683 | \$ 8,930 |

12. Financing

The following table presents a breakdown of Southern’s financing expenses:

| | Three months ended | | Six months ended | |
|---------------------------------|--------------------|---------------|------------------|---------------|
| | June 30, | | June 30, | |
| | 2024 | 2023 | 2024 | 2023 |
| Credit facility interest | \$ 671 | \$ 370 | \$ 1,268 | \$ 571 |
| Convertible debentures interest | 63 | 63 | 126 | 126 |
| Interest income | (10) | (22) | (19) | (174) |
| Accretion | 33 | 166 | 172 | 309 |
| Interest on lease obligations | 3 | 6 | 6 | 13 |
| Total Financing Expenses | \$ 760 | \$ 583 | \$ 1,553 | \$ 845 |

13. Capital Risk Management

The Company monitors its capital based on projected cash flow from operations and anticipated capital expenditures. In order to manage its capital structure, the Company prepares annual capital expenditure and operating budgets, which are updated as necessary. The annual and updated budgets are prepared by the Company’s management and approved by or reviewed with the Company’s Board of Directors. The budget results are regularly reviewed and updated as required.

In order to maintain or adjust the capital structure, the Company may issue shares, seek debt financing and adjust its capital spending to manage its current and projected capital structure. The Company’s ability to raise additional debt or equity financing is impacted by external conditions, including future commodity prices and global economic conditions. The Company continually monitors business conditions including changes in economic conditions, the risk of its drilling programs, forecasted commodity prices, and potential corporate or asset acquisitions.

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14. Commitments

The following table lists the Company's contractual obligations and commitments as at June 30, 2024:

| | Total | 2024 | 2025 | 2026 | 2027 | Thereafter |
|---------------------------------------|------------------|-----------------|-----------------|------------------|---------------|--------------|
| Long-term debt ⁽¹⁾ | \$ 17,119 | \$ 1,007 | \$ 4,028 | \$ 12,084 | \$ - | \$ - |
| Convertible debentures ⁽²⁾ | 3,131 | - | 3,131 | - | - | - |
| Lease obligations ⁽³⁾ | 576 | 58 | 93 | 174 | 174 | 77 |
| Total | \$ 20,826 | \$ 1,065 | \$ 7,252 | \$ 12,258 | \$ 174 | \$ 77 |

Notes:

- (1) Long-term debt consists of the Credit Facility – see note 5 – Long-term Debt for more information
- (2) Debentures have a maturity date of June 30, 2025.
- (3) The lease obligations relate to the Canadian office lease that is accounted for under IFRS 16.

On May 27, 2024, Southern entered into a new office space lease for a term of three years, with the option for one extension period for an additional three years. The new lease commences on December 1, 2024, the day after the current office lease expires.